DRN-4695866

The complaint

Mrs L complains Specialist Motor Finance Limited (SMFL) irresponsibly entered into a hire purchase agreement because it didn't complete reasonable and proportionate checks to ensure the agreement was affordable for her.

What happened

Mrs L entered into the hire purchase agreement with SMFL in September 2019 to acquire a used car. The cash price of the car was £11,424. Mrs L didn't pay a deposit and the total amount payable under the agreement was £20,708.80. She was to pay 59 equal monthly instalments of £344.98 and a final instalment of £354.98 (this included an option to purchase fee of £10).

Mrs L is represented in her complaint but for ease of reading I'll simply refer to Mrs L throughout this decision. Mrs L complained to SMFL on 22 September 2023 about irresponsible lending.

SMFL responded to the complaint on 16 November 2023. It felt it had completed reasonable and proportionate checks and the lending decision had been a fair one. Mrs L remained unhappy and asked our service to investigate.

Our Investigator issued a view explaining why they felt the checks hadn't been reasonable or proportionate. They went on to explain why they felt such checks would have shown the agreement wasn't affordable. Mrs L accepted the view. However, SMFL didn't respond to say whether they accepted our Investigator's view. Therefore, the case has been passed to me to decide.

What I've decided – and why

I've considered all the available evidence and arguments to decide what's fair and reasonable in the circumstances of this complaint.

The Financial Conduct Authority (FCA) sets out in a part of its handbook known as CONC what lenders must do when deciding whether or not to lend to a consumer. In summary, a firm must consider a customer's ability to make repayments under the agreement without having to borrow further to meet repayments or default on other obligations, and without the repayments having a significant adverse impact on the customer's financial situation.

CONC says a firm must carry out checks which are proportionate to the individual circumstances of each case.

Did SMFL complete reasonable and proportionate checks to satisfy itself that Mrs L would be able to repay the agreement in a sustainable way?

SMFL said it assessed Mrs L's affordability by using a combination of data sourced from Credit Reference Agencies (CRA), Office of National Statistics (ONS) and industry publications. It considered her net monthly income, credit commitments and non-discretionary expenditure to determine disposable income.

SMFL said it factored in all active debts and historic defaulted debts. It identified Mrs L had credit commitments of £122.91 and net income of £1,602. It said it calculated her non-discretionary spend at around £707.01. Taking into account a small buffer, this left her with around £747.08 disposable which meant it found the agreement was affordable for her.

In respect of Mrs L's credit history SMFL said Mrs L had five active credit items (four of which were up to date), and she had one good settled credit item. Also, five defaults which had occurred more than nine months prior to the credit application. Looking at the credit search, I can see a communication account was in arrears and there was a remaining balance of £1,018. Mrs L also had missed payments for her mortgage account, although it seems to have been brought up to date by the time of the lending.

Additionally, from the credit search and information I've been provided I can see Mrs L also had seven County Court Judgments (CCJs), the most recent of which was recorded two months prior to the agreement. I'm mindful she also had an account in arrears at the time. This shows Mrs L had previously been in financial difficulties, this was recent to the lending decision and her financial difficulties might still be ongoing. So, this should have prompted further checks to ensure Mrs L could meet her financial commitments.

Overall, I'm not satisfied the checks carried out were reasonable or proportionate here. Mrs L had CCJs recorded shortly before the lending decision and there was evidence of missed payments and arrears. Therefore, SMFL should have done more to determine her specific non-discretionary spend. Because of the adverse information, it wasn't reasonable to rely on ONS data as it had information to suggest Mrs L wasn't the average customer and that there might have been something more going on with her finances. This ought to have prompted further checks and verification of her financial circumstances.

Would reasonable and proportionate checks have shown that Mrs L would be able to repay the agreement in a sustainable way?

As I don't think reasonable and proportionate checks were carried out, I've gone on to consider what such checks were likely to have shown. To consider this, I've reviewed some bank statements provided by Mrs L and which cover the period leading up to the lending decision. For clarity, I'm not saying SMFL necessarily needed to obtain bank statements in order to complete reasonable and proportionate checks. However, the bank statements do show what information SMFL were likely to have obtained had it carried out such checks at the time of the agreement.

I've reviewed the bank statements and I'm satisfied Mrs L's income fell around the figure which had been verified by SMFL. Mrs L seemed to expect to receive around £1,622 on average.

From the statements, I can see there were repayments to loans and failed direct debits which weren't paid. She also seemed to try and make some larger payments to meet arrears. Therefore, it's more difficult to determine Mrs L's exact committed spend each month. So, I've weighed up the evidence I have in order to decide what I think reasonable and proportionate checks were most likely to have shown SMFL about Mrs L's committed expenditure.

I would also note some expenditure which I can't see, for example, there aren't payments towards bills such as gas, water and electric. However, Mrs L withdrew cash each month and she has explained around £300 went towards bills. She said the other amounts withdrawn went towards food, petrol and repaying council tax arrears. I find Mrs L's explanation plausible given the sums involved and because some expected expenses aren't included on the statements.

I'm satisfied the information shows her average committed expenditure before entering the agreement was around £1,476. This includes things such as her committed direct debits, food, petrol, insurance payments and credit commitments. It also includes her mortgage repayment and a proportion of the cash withdrawals which seem to have been for regular non-discretionary spend and were likely to have been necessary throughout the agreement. Taking into consideration the size of the monthly repayments (£344.98), it's clear her income of around £1,622 wasn't sufficient to meet her commitments and the new monthly repayment amount.

Notwithstanding this, Mrs L had a number of failed direct debits and seems to have been in arrears with a communications agreement. I can see she took out some additional lending and she has explained this was to pay off some of the arrears which had built up. I'm also mindful she had a CCJ recorded only two months prior to entering the agreement (July 2019). Taking into consideration all of the circumstances, I think it might well have been concluded that Mrs L was struggling to meet the commitments she already had, and it wouldn't have been responsible to extend further lending to her as it seems it was likely to have worsened her financial position.

Overall, I don't think reasonable and proportionate checks were carried out. I'm satisfied such checks would have shown the agreement wasn't affordable for Mrs L. Not only was she in arrears with her communications account, but it doesn't seem she had sufficient disposable income to cover her financial commitments as well as the monthly repayments under the agreement. Therefore, I don't think SMFL should have approved the lending here.

Putting things right

Mrs L sold the car to a third party and the proceeds were used to settle the finance. By this time, it seems Mrs L had already paid more than the cash price of the car towards the agreement and had been in possession of the car for around 45 months. Having reviewed the case, I think SMFL should put things right in a different way to what was set out by our Investigator.

I shared my thoughts with both parties before making a final decision. I said Mrs L should only have to pay the original cash price of the car, being £11,424. Anything which has been paid towards the agreement in excess of that amount should be refunded as an overpayment. I gave both parties the opportunity to comment. Mrs L accepted this, but I didn't receive a response from SMFL.

Having considered everything, I'm satisfied this is fair and reasonable in all the circumstances of this complaint. For the avoidance of doubt, payments made towards the agreement includes money which may have been paid directly to SMFL by the third party who purchased the vehicle and sent funds to settle the agreement.

Therefore, Specialist Motor Finance Limited should do the following to put things right:

- Refund any payments made towards the agreement made in excess of £11,424, representing the original cash price of the car. It should add 8% simple interest per year* from the date of each overpayment to the date of settlement.

- Remove any adverse information on Mrs L's credit file regarding the agreement.

* If SMFL considers that it's required by HM Revenue & Customs to deduct income tax from that interest, it should tell Mrs L how much it's taken off. It should also give Mrs L a tax deduction certificate if she asks, so she can reclaim the tax from HM Revenue & Customs if appropriate.

I've also considered whether the relationship might have been unfair under s.140a of the Consumer Credit Act 1974. However, I'm satisfied the redress I have directed above results in fair compensation for Mrs L in the circumstances of her complaint. I'm satisfied, based on what I've seen, that no additional award would be appropriate in this case.

My final decision

For the reasons outlined above, I'm upholding the complaint and Specialist Motor Finance Limited should put things right in the way outlined above.

Under the rules of the Financial Ombudsman Service, I'm required to ask Mrs L to accept or reject my decision before 25 July 2024.

Laura Dean
Ombudsman